

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF LEWIS SANITATION)	
COMPANY, INC. – GARDEN HEIGHTS)	
SEWER SYSTEM FOR ADJUSTMENT OF)	CASE NO.
RATES PURSUANT TO THE)	2005-00036
ALTERNATIVE RATE FILING)	
PROCEDURE FOR SMALL UTILITIES)	

O R D E R

On February 4, 2005, Lewis Sanitation Company, Inc. – Garden Heights Sewer System (“Lewis Sanitation”) filed its application for Commission approval of its proposed sewer rates. Commission Staff, having performed a limited financial review of Lewis Sanitation’s operations, has prepared the attached Staff Report containing Staff’s findings and recommendations regarding the proposed rates. All parties should review the report carefully and provide any written comments or requests for a hearing or informal conference no later than 10 days from the date of this Order.

IT IS THEREFORE ORDERED that all parties shall have no more than 10 days from the date of this Order to provide written comments regarding the attached Staff Report or requests for hearing or informal conference. If no request for a hearing or informal conference is received, this case will be submitted to the Commission for a decision.

Done at Frankfort, Kentucky, this 15th day of March, 2005.

By the Commission

ATTEST:


Executive Director

STAFF REPORT

LEWIS SANITATION – GARDEN HEIGHTS SEWER SYSTEM

CASE NO. 2005-00036

Pursuant to a request by Lewis Sanitation Company, Inc. – Garden Heights Sewer System (“Lewis Sanitation”) for assistance with the preparation of a rate application for its sewer operations, Commission Staff (“Staff”) performed a limited financial review of Lewis Sanitation’s test year operations for the calendar year ending December 31, 2003. The scope of Staff’s review was limited to obtaining information as to whether the test period operating revenues and expenses were representative of normal operations. Insignificant or immaterial discrepancies were not pursued and are not addressed herein.

Upon completion of the review, Staff assisted Lewis Sanitation in the preparation of a rate application. The application included an adjusted pro forma operating income statement, as shown in Attachment B to this report, wherein adjustments were made to test year operating revenues and expenses that were known and measurable and deemed to be reasonable. The rates proposed by Lewis Sanitation were based on the pro forma income statement shown in the application. The application also includes the calculation of Lewis Sanitation’s revenue requirement using an 88% operating ratio, which is frequently used by the Commission to determine revenue requirements for small utilities. To generate the revenue requirement of \$21,970, Lewis Sanitation is proposing to increase its annual revenue by \$7,714, an increase of 54% over normalized revenue of \$14,256. Lewis Sanitation’s proposed increase is high in percentage terms, but several factors are worth noting. First, Commission records

indicate Lewis Sanitation's present owners have operated the system since 1986 without a rate increase. Since then, costs for sludge hauling, transportation, and other expenses have increased consistent with the overall economy. Second, Lewis Sanitation has been charging only \$11.00 per month, a low rate compared with other Kentucky sewer utilities. Third, Lewis Sanitation's owners have been subsidizing the utility and postponing some expenditures in order to maintain low rates, and they are entitled to rates which provide them fair compensation and allow for adequate maintenance and repairs.

On February 4, 2005, Lewis Sanitation filed its rate application to the Commission for consideration. Staff is hereby adopting the contents of Lewis Sanitation's application as its recommendation in this report as if fully set out herein. Jess Thompson is responsible for all revenue adjustments and the calculation of the proposed rates. Jack Kaninberg is responsible for the determination of the revenue requirement. Based on the information included in Lewis Sanitation's application, Staff is of the opinion that the rates as shown in Attachment A of this report are reasonable and should be approved by this Commission.

Signatures

Prepared by: Jack Kaninberg
Financial Analyst, Water and Sewer
Revenue Requirements Branch
Division of Financial Analysis

Prepared by: Jess Thompson
Rate Analyst, Communications, Water,
and Sewer Rate Design Branch
Division of Financial Analysis

ATTACHMENT A
STAFF REPORT CASE NO. 2005-00036
STAFF'S RECOMMENDED RATES

Monthly Sewer Rate

Single Family Residential	\$16.96
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Lewis Sanitation Attachment B	2003	Adjustments	Ref.	Adjusted
Revenues (108 customers x \$11)	\$14,212	\$44	A	\$14,256
Owner/Manager. fee	\$1,301	\$2,299	B	\$3,600
Sludge Hauling	\$625	\$1,175	C	\$1,800
Water Cost	\$91	0		\$91
Other – Labor, Material, & Exp.	\$3,967	0		\$3,967
Rents	\$55	0		\$55
Fuel/Power for Pumping	\$2,246	0		\$2,246
Chemicals	\$275	0		\$275
Mt. Of Collection Sewer System	\$1,068	0		\$1,068
Mt. Of Treatment & Disposal	\$464	0		\$464
Admin & Gen. Salaries	0	\$1,200	D	\$1,200
Agency collection Fee	\$646	0		\$646
Uncollectible Accounts	\$77	0		\$77
Office Supplies and Other	\$1,341	(\$72) (\$513)	E	\$756
Outside Services Employed	\$575	0		\$575
Transportation Exp.	\$2,160	(\$1,080)	F	\$1,080
<i>Total Sewer O&M</i>	<i>\$14,891</i>	<i>\$3,009</i>		<i>\$17,900</i>
Depreciation Exp.	\$2,151	(\$1,737)	G	\$414
Amortization Exp.	\$839	(\$839) \$360	H	\$360
Taxes OT Income	\$122	0		\$122
Total Operating Exp.	\$18,003	\$793		\$18,796
Net Operating Income	(\$3,791)	(\$749)		(\$4,540)
Miscellaneous Nonoperating Income	\$198	(\$99)	I	\$99
<i>Net Income</i>	<i>(\$3,593)</i>	<i>(\$848)</i>		<i>(\$4,441)</i>

Calculation of Revenue Requirement using Operating Ratio Method:

\$18,796	Proforma Operating Expenses Before Income Taxes
<u>88%</u>	Operating Ratio
\$ 21,359	Revenue Requirement Before Tax
<u>(\$18,796)</u>	Proforma Operating Expenses
\$ 2,563	After Tax Net Income
<u>x 1.23839</u>	Tax Factor
\$ 3,174	Net Income Before Income Tax (Tax is \$611)

\$ 21,970	Revenue Requirement Including Tax
<u>(\$14,256)</u>	Normalized Revenues
\$ 7,714	Recommended Revenue Increase (54% increase)

\$21,970 / 12 = \$1,830.83 divided by 108 customers = \$16.852 rounded to \$16.96 per month

Explanatory Notes:

- A. Normalized Revenues based on 108 customers currently paying \$11.00 per month.
- B. The PSC normally allows an owner/manager fee of \$3,600 for operators of sewer utilities, and one is justified in this case.
- C. Sludge hauling expense based on monthly hauling at \$150 per load. This rate was increased from \$125 per load effective October 19, 2004. In addition, because of the utility's poor revenue streams, sludge hauling was not done in the past as often as it should be done.
- D. Proforma Administrative Salaries Expense of \$100 per month to compensate the owner's wife for her duties on behalf of the utility, including billing and other administrative tasks.
- E. Office Supplies Expense for 2003 included a \$72 payment for cell phone service unrelated to the utility. In addition, 33.3 percent of the telephone expense of \$769 at the owner's residence was allocated to the utility, with the remaining 66.7 percent allocated to personal and other business use.
- F. Transportation Expense of \$2,160 for the owner's truck was allocated 50 percent to the utility, and 50 percent to the owner's other business use.
- G. Proforma Depreciation Expense was adjusted to remove the approximately 80.75 percent of the Utility Plant In Service that was funded by Contributions in Aid of Construction.
- H. Amortization Expense was adjusted to exclude the amortization expense of \$839 related to an acquisition adjustment, and to include the 5-year amortization of an EPA permit costing \$1,800.
- I. Miscellaneous Nonoperating Income of \$198 was reduced by 50 percent because a Kenergy capital credit of \$198 is not expected to recur annually.